

EXAM REVIEW

ACCOUNTING 101 - UNIT III - CHAPTERS 7, 8 & 9

STUDY SUGGESTIONS

Review your class notes, homework exercises and problems.

Be sure to review any chapter appendices assigned on the General Course Outline.

Review **Demonstration Problem, Summary and Key Terms** at the end of each chapter.

Answer the **Multiple Choice Quiz** at the end of each chapter.

Answer **Multiple Choice Quiz A and B** on the textbook website www.mhhe.com/wild .

Know accounting terms and concepts by answering the **Discussion Questions** at the end of each chapter.

Know the account classification (i.e. asset, liability, or owner's equity) and normal balance of all accounts.

Know the what the financial ratios mean and how to calculate them.

Other online help is available at a variety of sites such as:

<http://www.cliffsnotes.com/WileyCDA/Section/id-305261.html>

<http://www.simplestudies.com/>

Chapter 7 – Accounting for Receivables

Explain the difference between the direct write-off method and the allowance method.

Journalize the entries for the allowance method of accounting for uncollectible accounts.

Estimate uncollectible accounts expense based on sales and based on an analysis (aging) of receivables.

Journalize the entries for the direct write off of uncollectible receivables.

Journalize the entries for the write off of uncollectible receivables using the allowance method.

Journalize the entries for notes receivable transactions.

Journalize the entries to write off of dishonored notes receivable.

Journalize accrued interest revenue prior to maturity date.

Calculate interest revenue at the maturity date and at an interim date, the term of the note and the maturity date of the note.

Know the different methods of selling receivables.

Compute days' sales outstanding (uncollected) and accounts receivable turnover.

Chapter 8 - Accounting for Long-Term Assets

Know how to determine the cost of long-term assets.

Know how to classify fixed asset costs as either capital expenditures or revenue expenditures (operating expenses).

Compute depreciation expense the using straight-line, the units-of-production, and the declining-balance methods.

Adjust depreciation expense calculations when the asset is owned for less than a full year (partial year depreciation).

Compute and journalize adjustments to depreciation for changes in estimates, such as salvage value or useful life.

Compute depletion expense and journalize the entry for depletion of natural resources.

Journalize entries for acquiring and amortizing intangible assets, such as patents and copyrights.

Journalize entries for the disposal of fixed assets:

- Discarding assets

- Selling assets

- Exchanging assets for similar assets

Compute total asset turnover.

Chapter 9 – Accounting for Current Liabilities

Liabilities are probable future payments for which there are current obligations to pay due to the occurrence of past events.

Understand the difference between current and long-term liabilities.

Understand the different types of current liabilities:

- Determinable - known and determinable in amount

- Estimated – known and the amount can be reasonably estimated

- Contingent - depends upon a probable future event occurring; amount may be known or reasonably estimated

Journalize employer payroll taxes and employee payroll deductions.

Journalize the entries for notes payable transactions.

Journalize accrued interest expense prior to maturity date.

Calculate interest expense at the maturity date and at an interim date, the term of the note and the maturity date of the note.

Journalize other accrued liabilities such as warranties, vacation, bonus and deferred revenue.

Compute the times interest earned ratio.

SAMPLE PROBLEMS

Problem 1 - Uncollectible Receivables

- a. What are the two methods of accounting for uncollectible receivables?
- b. What is the journal entry used to write-off an uncollectible account when using the direct write-off method?
- c. What is the journal entry used to write-off an uncollectible account when using the allowance method?
- d. What is the journal entry used to reinstate an account when using the direct write-off method?
- e. What is the journal entry used to reinstate an account when using the allowance method?
- f. What are the two methods used to estimate uncollectible accounts expense when using the allowance method?

Problem 2 - Estimated uncollectible amounts based on sales

Before year-end adjustment, the Allowance for Doubtful Accounts has a credit balance of \$25,000. Uncollectible accounts are estimated as 1% of credit sales, which were \$1,500,000. The accounts receivable balance is \$325,000.

- a. What is the uncollectible accounts expense for the period?
- b. What is the journal entry required?
- c. What is the balance of the Allowance for Doubtful Accounts after adjustment?
- d. What is the net realizable value of the receivables after adjustment?

Problem 3 - Estimated uncollectible amounts based on analysis (aging) of receivables

Before the year-end adjustment the Allowance for Doubtful Accounts has a debit balance of \$5,000. Using the aging of receivables method, the desired balance of the Allowance for Doubtful Accounts is estimated as \$35,000.

- a. What is the uncollectible accounts expense for the period?
- b. What is the journal entry required?
- c. What is the balance of the Allowance for Doubtful Accounts after adjustment?
- d. If the accounts receivable balance is \$325,000, what is the net realizable value of the receivables after adjustment?

Problem 4 - Entries for receipt and dishonor of note receivable

A 60-day, 12% note for \$15,000, dated March 1 is received from a customer on account. The maker dishonors the note at maturity.

- a. What is the journal entry to record the receipt of the note?
- b. What is the maturity date of the note?
- c. What is the maturity value of the note?
- d. What is the journal entry to record the dishonor of the note receivable?

Problem 5 - Compute Accounts receivable turnover and the number of day's sales in receivables

The Nicholas Company had net sales on account of \$6,570,000 during 1998. The beginning and ending accounts receivable were \$475,000 and 535,000 respectively.

- a. Compute accounts receivable turnover for 1998

- b. Compute the number of days' sales in receivables at year-end.

Problem 6 - Straight-line depreciation

A machine with a cost of \$50,000 has an estimated residual value of \$5,000 and an estimated useful life of 5 years.

What is the amount of annual depreciation computed by the straight-line method?

Problem 7 - Depreciation by the units-of-production method

A truck that cost \$40,000 has a residual value of \$5,000 and an estimated useful life of 100,000 miles.

- a. Compute the depreciation rate per mile.
- b. Compute the first year's depreciation if the truck was driven 12,000 miles?

Problem 8 - Depreciation by the declining-balance method

Production equipment acquired at the beginning of the year at a cost of \$85,000 has an estimated residual value of \$10,000 and an estimated useful life of 10 years. It is depreciated using the declining-balance method at twice the straight-line rate.

- a. What is the depreciation expense for the first year?
- b. What is the depreciation expense for the second year?

Problem 9 - Disposal of fixed asset

A metal stamping machine acquired on January 1, 1990 at a cost of \$ 55,000 had an estimated residual value of \$ 5,000 and an estimated life of 10 years. It was sold on July 1, 1998 for \$ 10,000.

- a. What was the annual depreciation using the straight-line method?
- b. What was the book value on July 1, 1998 when it was sold?
- c. Journalize the entry to record the sale, including the depreciation for the current year.

Problem 10 - Asset trade for similar asset

A truck with a cost of \$35,000 and accumulated depreciation of \$32,500 is traded for a new truck priced at \$ 45,000 with a trade-in allowance of \$ 5,000.

- a. What is the book value of the old truck?
- b. What is the cost of the new truck for financial reporting purposes?
- c. What is the journal entry to record the purchase?

Problem 11 - Asset traded for a similar asset

A truck with a cost of \$35,000 and accumulated depreciation of \$ 30,000 is traded for a new truck priced at \$ 45,000 with a trade-in allowance of \$ 2,500.

- a. What is the book value of the old truck?
- b. What is the cost of the new truck for financial reporting purposes?
- c. What is the journal entry to record the purchase?

Problem 12 - Depletion entries

Bosch Company acquired mineral rights for \$15,000,000. The mineral deposit is estimated at 60,000,000 tons. During the current year 11,500,000 tons were mined and sold for \$3,500,000.

- a. Determine the amount of depletion expense for the current year.
- b. Journalize the adjusting entry to recognize the expense.

Problem 13 - Amortization of patent rights

On January 2, 1998, the Jackson Corporation acquired patent rights from the Cooper Company for \$85,000, incurring legal costs of \$5,000. Although the patent will not expire for 17 years, its estimated useful is only 15 years.

Journalize the entry to amortize the patent at the end of the current fiscal year.

Problem 14 - Classifying liabilities

Axis Company has the following liabilities on its trial balance:

- Notes Payable due in 7 months
- Wages Payable
- Mortgage Payable due in 10 years
- Note payable due in 15 moths payable monthly
- FICA Taxes Payable

Classify each liability as either current or long-term.

Problem 15 – Contingent Liabilities

Jones Inc. is the defendant in two lawsuits. They expect to lose the first case and estimate that the damages will be approximately \$1,000,000. Although they expect to prevail in the second case, the damages will be approximately \$500,00 if they lose. Identify which lawsuit(s) should be recorded as a liability and the reason for the liability.

Problem 16 – Deferred Revenue

As of October 31, a concert promoter received \$5,000,000 for advance ticket sales for a series of four concerts beginning November 5. Record the journal entries for October 31 and for the second concert on November 6.

Problem 17 – Income Taxes

Snively Company accrues income taxes each quarter based on the expected tax rate for the year. Through September (9 months), income before income taxes was \$1,000,000 and the estimated tax rate was 30%. Snively had an excellent 4th quarter, and by December 31, income before income taxes had doubled. The tax rate had increased to 40% for the year. The taxes will be paid during January of the following year. Prepare the journal entry Snively should record on December 31.

Problem 18 - Entries for a note payable

The company purchases inventory using a 60-day, 12% note for \$15,000, dated December 1. The maker honors the note at maturity.

- a. What is the journal entry to record the issuance of the note?
- b. What is the maturity date of the note?
- c. What is the maturity value of the note?
- d. What is the journal entry on December 31?
- e. What is the journal entry on the maturity date?

SOLUTIONS TO SAMPLE PROBLEMS

Problem 1

a. The two methods of accounting for uncollectible receivables are the direct write-off method and the allowance method.

b. The journal entry used to write-off an uncollectible account when using the direct write-off method:

Uncollectible Accounts Expense	Debit	
Accounts Receivable		Credit

c. The journal entry used to write-off an uncollectible account when using the allowance method:

Allowance for Doubtful Accounts	Debit	
Accounts Receivable		Credit

d. The journal entry used to reinstate an account when using the direct write-off method:

Accounts Receivable	Debit	
Uncollectible Accounts Expense		Credit

e. The journal entry used to reinstate an account when using the allowance method:

Accounts Receivable	Debit	
Allowance for Doubtful Accounts		Credit

f. The two methods used to estimate uncollectible accounts expense when using the allowance method are the **estimate based on sales** and the **estimate based on analysis of receivables**.

Problem 2

a. The uncollectible accounts expense for the period is \$15,000 (1% of \$1,500,000)

b. The journal entry required is:

Uncollectible Accounts Expense	15,000	
Allowance for Doubtful Accounts		15,000

c. The balance of the Allowance after adjustment is \$40,000. (25,000 + 15,000)

d. The net realizable value after adjustment is \$285,000. (325,000 - 40,000)

Problem 3

- a. The uncollectible accounts expense for the period is \$40,000 (35,000 + 5,000)
- b. The journal entry required is:
- | | | |
|---------------------------------|--------|--------|
| Uncollectible Accounts Expense | 40,000 | |
| Allowance for Doubtful Accounts | | 40,000 |
- c. The balance of the Allowance after adjustment is \$35,000
- d. The net realizable-value after adjustment is \$290,000. (325,000 - 35,000)

Problem 4

- a. The journal entry to record the receipt of the note is:
- | | | |
|---------------------|--------|--------|
| Notes Receivable | 15,000 | |
| Accounts Receivable | | 15,000 |
- b. The maturity date of the note is April 30.
- c. The maturity value of the note is \$15,300; (15,000 X. 12 X 60 / 360)
- d. The journal entry to record the dishonor of the note receivable is:
- | | | |
|---------------------|--------|--------|
| Accounts Receivable | 15,300 | |
| Cash | | 15,000 |
| Interest Revenue | | 300 |

Problem 5

- a. Accounts receivable turnover for 1998 was 13.0
 $6,570,000 / (475,000 + 535,000) / 2 = 13.0$
- b. The number of days' sales in receivables at year end was 29.7 days
 $535,000 / (6,570,000 / 365) = 29.7$

Problem 6 - Straight-line depreciation

$(50,000 - \$5,000) / 5 \text{ years} = \$9,000 \text{ per year}$

Problem 7 Depreciation by the units-of-production method

- a. $(\$45,000 - \$5,000) / 100,000 \text{ miles} = \0.35 per mile
- b. $12,000 \text{ miles} \times \$0.35 = \$4,200$

Problem 8 Depreciation by the declining-balance method

- a. First year: 20% of \$85,000 = \$17,000
- b. Second year: 20% of (\$85,000 - \$17,000) = \$13,600

Problem 9 - Disposal of fixed asset

- a. $(\$55,000 - \$5,000) / 10 \text{ years} = \$5,000 \text{ per year}$
- b. $\$55,000 - (8.5 \text{ years} \times \$5,000) = \$12,500$
- c. Depreciation Expense (for ½ year) 2,500
 Accumulated Depreciation-Equipment 2,500
 Cash 10,000
 Accumulated Depreciation-Equipment 42,500
 Loss on Disposal of Fixed Assets 2,500
 Equipment 55,000

Problem 10 - Asset traded for a similar asset

- a. The book value is \$2,500; $(\$35,000 - \$32,500)$
- b. The amount of cash paid is \$40,000; $(\$45,000 - \$5,000)$
- c. The cost of the new truck is: \$42,500; $(\$40,000 + \$2,500)$ (cash paid + book value of old truck)
- d. Truck (new) 42,500
 Accumulated Depreciation-Truck (old) 32,500
 Truck (old) 35,000
 Cash 40,000

Problem 11 - Asset traded for a similar asset

- a. The book value is \$5,000; $(\$35,000 - \$30,000)$
- b. The amount of cash paid is \$42,500; $(\$45,000 - \$2,500)$
- c. The cost of the new truck is: \$45,000; $(\$42,500 + \$5,000 - \$2,500)$
 Cost of new truck = book value of old truck + cash paid - loss on trade-in
- d. Truck (new) 45,000
 Accumulated Depreciation-Truck (old) 30,000
 Loss on Disposal of Fixed Assets 2,500
 Truck (old) 35,000
 Cash 42,500

Problem 12 - Depletion entries

- a. $\$15,000,000 / 60,000,000 = \0.25 per ton
 $11,500,000 \times \$0.25 = \$2,875,000 \text{ depletion expense}$
- b. Depletion Expense 2,875,000
 Accumulated Depletion 2,875,000

Problem 13 - Amortization of patent rights

Amortization Expense - Patents	6,000	
Accumulated Amortization - Patents		6,000

Problem 14 - Classifying liabilities

Current

- Notes Payable due in 7 months
- Wages Payable
- FICA Taxes Payable
- First year of Mortgage Payable due in 10 years
- First 12 months of Note payable due in 15 months payable monthly

Long-term

- Final 9 years of Mortgage Payable due in 10 years
- Final 3 months of Note payable due in 15 months payable monthly

Problem 15 – Contingent Liabilities

Although the amount of damages can be estimated for both lawsuits, only the first case should be recorded as a liability since there is a high probability of loss. The second case should be disclosed in the footnotes to the financial statements.

Problem 16 – Deferred Revenue

Oct. 31	Cash	5,000,000	
	Unearned Ticket Revenue		5,000,000
Nov. 6	Unearned Ticket Revenue	1,250,000	
	Earned Ticket Revenue		1,250,000

Problem 17 – Income Taxes

Taxes for the year:	$\$2,000,000 \times 40\% = \$800,000$	
Taxes through September:	$\$1,000,000 \times 30\% = \underline{\$300,000}$	
4 th quarter tax expense	$\$500,000$	
	Income tax expense	500,000
	Income taxes payable	500,000

Problem 18 - Entries for a note payable

a. The journal entry to record the receipt of the note is:

Inventory	15,000	
Notes payable		15,000

b. The maturity date of the note is January 30.

c. The maturity value of the note is \$15,300; $(15,000 \times .12 \times 60 / 360)$

d. The journal entry to record the dishonor of the note receivable is:

Interest expense	150	
Interest payable		150

e. The journal entry to record payment of the note on January 30 is:

Notes payable	15,000	
Interest expense	150	
Interest payable	150	
Cash		15,300